

Message Text

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PAGE 01 EC BRU 00678 221934Z

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SUBJECT: EC COMMISSION REACTION TO ITALIAN EXCHANGE MARKET
ANNOUNCEMENTS

REF: ROME 978

1. BEGIN SUMMARY: THE EC COMMISSION DOES NOT PLAN ANY IMMEDIATE MEASURES TO ASSIST ITALY IN ITS CURRENT FINANCIAL CRISIS. COMMISSION OFFICIALS BELIEVE, HOWEVER, THAT CHANCES HAVE INCREASED THAT THE EC WILL MAKE A BORROWING ON THE EURO-DOLLAR MARKET FOR ITALY. SHOULD PRESSURE INTENSIFY AGAINST THE FRENCH FRANC, OFFICIALS HERE SPECULATE THAT THE GOF MAY TEMPORARILY LEAVE THE EUROPEAN MONETARY SNAKE. END SUMMARY.

2. THE COMMISSION PRESS SPOKESMAN SAID ON JANUARY 22 THAT THE ITALIAN FINANCIAL SITUATION WAS NOT CATASTROPHIC AND THERE WAS NO REASON TO DRAMATIZE IT. COMMISSION OFFICIALS SAY PRIVATELY THAT THE GOI HAS NOT CONTRAVENED ANY EC REGULATIONS AND NO EC RESPONSE TO THE GOI EXCHANGE RATE MEASURES IS CURRENTLY PLANNED. OFFICIALS HERE ARE PARTICULARLY RELIEVED TO LEARN THAT THE GOI DOES NOT PLAN TO TAKE ANY MEASURES TO RESTRAIN ITALIAN IMPORTS.

3. COMMISSION FINANCIAL OFFICIALS SAY THE GOI ANNOUNCEMENT OF
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PAGE 02 EC BRU 00678 221934Z

WITHDRAWING SUPPORT FOR THE LIRE AND DISCONTINUING THE DAILY

FIXING OF THE LIRE RATE IS PRIMARILY AN EFFORT TO PUT PRESSURE ON SOME ITALIAN POLITICAL FRACTIONS TO ORGANIZE PROMPTLY A NEW GOVERNMENT. OFFICIALS HER NOTE THAT THE GOI COULD HAVE QUIETLY WITHDRAWN SUPPORT FOR THE LIRE AND ALLOWED THE LIRE TO FLOAT FREELY WITHOUT ANY PUBLIC ANNOUNCEMENT. THE COMMISSION ASKED MEMBERS OF THE EC MONETARY COMMITTEE IF THEY WANTED TO HOLD AN EMERGENCY MEETING. THE COMMITTEE DECIDED NOT TO MOVE UP ITS NEXT SCHEDULES MEETING OF JANUARY 31 AT WHICH TIME THE ITALIAN SITUATION WILL BE DISCUSSED.

4. COMMISSION OFFICIALS BELIEVE THE EC WILL NOW INTENSIFY ITS EFFORTS TO USE THE EC COMMON BORROWING FACILITY TO OBTAIN A LOAN OF ABOUT ONE BILLION DOLLARS FOR ITALY FROM A BANK CONSORTIUM. THIS BORROWING WOULD PROBABLY BE ON THE EURODOLLAR MARKET AT A VARIABLE INTEREST RATE. THE RATE WOULD BE ADJUSTED EVERY SIX MONTHS OR ANNUALLY; THE LOAN WOULD BE REVIEWABLE, PROBABLY EXTENDING OVER A FIVE YEAR PERIOD. SEVERAL MEMBER STATES, ESPECIALLY THE FRG, HAVE EXPRESSED CONCERN OVER A BORROWING INVOLVING AN ADJUSTABLE INTEREST RATE, OFFICIALS HERE SPECULATE THAT BECAUSE OF ITALY'S PRESSING FINANCIAL NEEDS THERE WILL NOW BE SUPPORT FOR SUCH A BORROWING. OFFICIALS ADD THAT THERE IS NO OTHER EC CREDIT FACILITY FROM WHICH THE GOI MIGHT BORROW. ITALY HAS ALREADY USED MOST OF ITS CEILING UNDER THE MEDIUM-TERM FACILITY. THE GOI HAS A REMAINING RESIDUAL OF ABOUT \$300 MILLION IN THIS FACILITY, BUT COMMISSION OFFICIALS BELIEVE THE UK AND FRANCE WOULD HAVE PROBLEMS IF THE GOI TRIED TO DRAW ON THIS RESIDUAL.

5. COMMISSION OFFICIALS ADD THAT DURING 1975 ITALY SUCCESSFULLY MAINTAINED A STABLE, EFFECTIVE EXCHANGE RATE FOR THE LIRE ON A TRADE-WEIGHTED BASIS. ITS INTERVENTION POLICY WAS IN PART DESIGNED TO REDUCE INFLATIONARY PRESSURE THAT WOULD BE CREATED BY FURTHER DEPRECIATION OF THE LIRE. SHARP DEPRECIATION OF THE LIRA NOW COULD CREATE TRADE COMPETITION PROBLEMS FOR OTHER EC MEMBERS, ESPECIALLY FRANCE. COMMISSION OFFICIALS DO NOT BELIEVE THAT THE GOF CURRENTLY PLANS TO CHANGE THE PIVOT RATE OF THE FRANC IN THE EUROPEAN MONETARY SNAKE. HOWEVER, SHOULD SPECULATION INTENSIFY AND RUN AT A LEVEL OF ABOUT \$500 MILLION PER DAY FOR A WEEK OR MORE, THE GOF MAY HAVE TO RECONSIDER THIS POSITION. OFFICIALS HERE SAY GOF NET INTERVENTIONS ON JANUARY 21 AMOUNTED TO ABOUT \$300 MILLION AND SPECULATIVE PRESSURE APPEARS TO BE INTENSIFYING.

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PAGE 03 EC BRU 00678 221934Z

6. SHOULD THE GOF BE FORCED TO CHANGE THE FF RATE, MOST OFFICIALS HER SPECULATE THAT FRANCE WOULD LIKELY TEMPORARILY LEAVE THE SNAKE AND ALLOW THE FRANC TO FLOAT. ONCE A NEW EQUILIBRIUM RATE WAS ESTABLISHED, THE GOF WOULD ASK TO RE-ENTER THE SNAKE. OFFICIALS ADD THAT GISCARD MADE THE DECISION TO RE-ENTER THE SNAKE IN ORDER TO DEMONSTRATE FRENCH SUPPORT OR EC SOLIDARIY IN THE MONETARY FIELD. THEY BELIEVE THE GOF WILL WANT TO CONTINUE ITS

SUPPORT FOR THE SNAKE.
GREENWALD

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